

## Gains to Chinese Bidder Firms:

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DOI:

[10.1111/j.1468-036X.2013.12031.x](https://doi.org/10.1111/j.1468-036X.2013.12031.x)

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*Document Version*

Peer reviewed version

*Citation for published version (Harvard):*

Black, E, Doukas, A, Xing, X & Guo, J 2015, 'Gains to Chinese Bidder Firms: Domestic vs. Foreign Acquisitions', *European Financial Management*, vol. 21, no. 5, pp. 905-935. <https://doi.org/10.1111/j.1468-036X.2013.12031.x>

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# Gains to Chinese Bidder Firms: Domestic vs. Foreign Acquisitions

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## ABSTRACT

This paper examines whether foreign acquisitions of Chinese firms improve share-price performance relative to domestic acquisitions, controlling for firm size and target industry. The results show that foreign acquisitions do not enjoy positive short-run market reactions but do realize significant long-run profits when the acquiring firm is large. Additionally, addressing anecdotal evidence, while resource-related acquisitions generate significant gains in the short-run, driven mainly by domestic deals, significant reversals are found long-term. International investment is shown to be on an upward trend for China and can be lucrative for large organizations.

*JEL Classification:* G14; G34.

**Keywords:** Merger and Acquisitions, China, Financial Performance, Scarcity, Cross-Border, Foreign Direct Investment, Multinational, Diversification

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Comments received throughout the formulation of this work are gratefully acknowledged. Special thanks go to John Doukas, an anonymous referee as well as the participants of the 2011 EFMA Asian Financial Management Symposium for valuable comments and suggestions received throughout this work.

## 1. Introduction

China has catapulted onto the global socio-economic landscape at a rapid pace in recent times. Globalization and financial market integration has led China to become a central and integral part of the world's economic landscape, igniting a plethora of political concerns. Zhou et al. (2012) show that the Chinese government has increasingly sought to recommend firms to acquire foreign targets with menacing alacrity so as to boost both the technological advancement and subsequent economic growth of this emerging economy. However, instead of the oft-eulogized invisible hand of Adam Smith, Chinese firms are facing a multitude of diverse international hands, each actively trying to block completion of Chinese foreign acquisitions. This protectionist display against Chinese acquirers arguably heightens the importance that these firms display unfaltering judgment throughout the selection, acquisition and integration process in pursuit of their chosen target. The relevant literature is scarce while the wider existing work related to mergers and acquisitions in general is virtually redundant when faced with the unique idiosyncrasies regarding the performance of Chinese firms engaged in foreign acquisitions relative to domestic ones. We aim to fill this gap by examining the short-term market reaction to the merger announcements of Chinese acquirers as well as their long-term post-merger share price performance, stratifying the sample according to whether the target is domestic or foreign.

Since the economic reform of 1978, China has cultivated a high economic growth rate to become the world's second-largest economy, valued at a staggering £5.8 trillion (Flanders, 2011). During this time, domestic companies such as Lenovo have grown substantially, moving into the international arena to compete with dominant Western brands such as Hewlett-Packard (Dietz, Orr and Xing, 2008). In 2011, foreign investment via merger activity rose by 96% when backed by private-equity, valued at \$12.3 billion, increasing from the \$6.3 billion spent during 2010 (Private Equity Asia, 2012).

However, the internationalization of Chinese firms has been no easy feat. Foreign acquisitions have exacerbated Western apprehension regarding the exchange of corporate control to the East particularly given the mainstream identity of targeted major international Western brands, such as IBM (Private Equity Asia, 2012) and Volvo (China Business News, 2012). Political radars have honed in on foreign acquisitions involving the People's Republic

of China<sup>1</sup>, particularly given that many involve the purchase of targets within the energy, industrials or technological sectors (The Economist, 2011-12) whereby growing demand and diminishing resources is heightening the implications of economic scarcity. As an example, the office of President Obama in the US has openly criticized trade practices with China. Indeed, the New York Times reported that the Obama administration has recommended that the Committee on Foreign Investment into the US should ‘*block any mergers and acquisitions involving the Chinese companies and American businesses*’ due to national security concerns (Schmidt et al. in New York Times, 2012).

While Chinese foreign acquisitions have led to a stream of journalistic articles (within The Economist, Financial Times and so forth), there have been few academic studies that have specifically examined Chinese acquisitions on a national versus international basis since 2000, with most research pertaining to the US (Jensen and Ruback, 1983; Shleifer and Vishny, 2003) or the EU (Faccio and Masulis, 2005). The historically insular Chinese economy has in fact only recently been popularized despite China exhibiting unique characteristics worthy of academic investigation for a number of decades. Some of these key characteristics are related to the level of state involvement and resultant political connectedness in the corporate decision-making process (see Gao and Kling, 2007; Xu et al., 2011; Wu et al., 2012; Zhou et al., 2012). While many papers focus on the unique political structure and its ramifications upon traditional firm performance measures, none to our knowledge has investigated the financial performance of bidders that acquire domestically versus those which decide acquire abroad.

Despite China receiving little attention in this field, there exists a plethora of literature which have centered on traditional US and EU datasets examining the value of firms acquiring abroad. The premise lies in whether or not investors place a premium upon international firms relative to domestic ones given the benefits of diversification within a multinational framework. In seminal work from the eighties, Doukas and Travlos (1988) argued that the primary motive for firm’s going abroad ‘*lies in the flexibility to transfer resources across borders through a globally maximizing network*’ (Doukas and Travlos, 1988: 1161). In this sense, multinational firms can earn a price premium via offering investors an ability to

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<sup>1</sup> For example, Swedish government officials strongly opposed the sale of Volvo to the Chinese car manufacturer Geely under the fear of the potential outflow of intellectual property to the East, resulting in the deal being referred to the European Commission on anti-trust grounds (Breaking News, 2010).

sidestep institutional restrictions and information externalities. Thus the acquisition of a foreign target can act as an information signal to the market regarding the firm's intention to a) expand globally and b) act to directly exploit capital market distortions. The study finds that multinational corporations from the US that do not operate in the country and/or industry of the target before the acquisition earn the most positive and significant gains, supporting the premise of indirect global diversification benefits.

In related work, Morck and Yeung (1991) suggest that cross-border acquisitions can offer firms an ability to enhance their value through the expansion of its operations abroad, specifically for those that possess valuable intangible assets (i.e. superior production skills, patents, marketing abilities, consumer goodwill and so forth), termed the internalization theory. Their results indicate support for the positive effects of valuable intangibles when acquiring abroad. Moreover, given the increasing trend for internationalization of emerging market firms, the *reverse internalization* hypothesis argues that it is the ability to acquire valuable intangible assets such as knowledge that could help explain the decision to buy abroad for BRIC organizations (Gubbi et al., 2010).

There are clear opportunities to contribute to, as well as to update, this seminal existing literature. It is of growing importance for China and the rest of the world to gain a deeper understanding of the financial performance of foreign acquisitions given the predictions that the future landscape of the global economy is set to become predominantly Chinese (Jacques, 2012). This would help to assess whether such investments are economically worthwhile for the Chinese economy that aims to foster continued high-level growth and development. Furthermore, it will also help to shed clarity upon Western concerns regarding the motivation of the Chinese bidder given economic scarcity, as evidenced with the stance of President Obama's office regarding US national security implications. Secondly, there are limited studies on offer that fully assess Chinese foreign direct investment (FDI) in terms of mergers and target characteristics. No study, to the best of our knowledge, has cross-examined the *positive multinational network* hypothesis of Doukas and Travlos (1988) relative to both the *internationalization* hypothesis of Morck and Yeung (1991) and the adjusted *reverse internalization* hypothesis (Gubbi et al., 2010) using a Chinese dataset.

With this in mind, we focus upon China and separate our sample of acquisitions by target nation in terms of whether the firm is located in mainland China ('**Domestic**') or not

(‘**Foreign**’). Using a comprehensive sample, we examine short-run announcement returns for bidders using a three-day event window as well as the long-term share-price performance, utilizing buy-and-hold (BHAR) methodology for a twenty-four month holding period with bootstrapped t-statistics so as to control for the possible skewness effect (see Barber and Lyon, 1997). Additionally, we adjust our analysis to control for the size of the bidder under the advocacy of Fama and French (1992). Secondly, we also investigate the performance of bidders stratified by the industry of the target to examine both the volume of deals within certain sectors as well as the profits being extracted.

The short-term results indicate that domestic transactions generate 2.76% (0.000) significant announcement returns - these positive returns hold regardless of the method of payment used - while foreign acquisitions lose -0.58% (0.604), statistically insignificant at any conventional level. Moreover, domestic acquirers statistically outperform cross-border ones by 2.45% (0.006). Additionally, the short-term analysis reveals that Chinese bidders earn significant abnormal returns when purchasing within the energy, industrials and materials sectors. However, these profits are confined to domestic transactions and thus Western political reactions regarding the supposed loss of economic resources towards the Far East are shown to be unfounded.

Over the long-term period, we find that domestic acquirers generate statistically significant losses of -7.98% (0.023) while foreign acquisitions generate insignificant returns of 14.20% (0.656) on the aggregate. However, when we control for firm-size, we find that there is a significantly positive long-run over-performance of 29.81% (0.006) for large foreign acquisitions benchmarked against domestic ones while large foreign acquisitions earn 22.39% (0.014) at the aggregate. This result suggests that there is a financial benefit for Chinese acquirers of going abroad so long as the firm is large enough to compete on the global market, consistent with the implications of *reverse internalization* whereby foreign acquisitions are enhancing the competitiveness of Chinese firms within the global economy.

This paper contributes to the existing literature in several key ways. Firstly, this is the first paper to our knowledge that empirically examines a comprehensive Chinese merger dataset in order to ascertain the contrasting market reaction to the announcement of domestic versus foreign transactions. Secondly, after controlling for firm size, we find large foreign acquisitions can generate significant long-term value for Chinese bidders. Finally, this work

shows that there has been a significant increase in the volume of cross-border investment via M&A activity emanating from China, with consolidation of key sectors such as energy and high-technology, indicating potential for a continued upward volume of transactions.

The paper continues as follows. Section 2 reviews the existing literature; Section 3 outlines the data and methodological approach; Section 4 discusses the results of the empirical analysis; and finally, Section 5 concludes the paper with ideas for further research.

## **2. Literature Review**

### **2.1. The Emergence of China**

By 2010, China had emerged to become the world's second largest economy overtaking Japan, despite still being a developing nation (Tenders Info, 2010). Simultaneously, promotion of foreign investment by the People's Republic of China has significantly influenced the expansion and restructuring of the domestic economy since the nineties, with the economic value and trading volume of M&A deals increasing year-on-year (Morck, Yeung and Zhao, 2008).

There have been a number of political reforms that have vastly shaped the Chinese economy, which serve as a foundation for the motivation of this work. In particular, the state implemented the "Go-Out" (sometimes termed "Go Global" policy) in 1999 to promote foreign acquisition activity, overseas investment and co-development agreements with foreign firms (Ma and Hurd, 2005). This policy has endured multiple reforms over the years as the state aims to refine a success strategy for international investment. Additionally, in 2001, the government set aside \$500 billion for overseas investments to be undertaken over a five-year period, directed at specific sectors, such as energy to acquire supplies of oil and gas (Ma and Hurd, 2005). Chinese firms should, under the new policy, seek to acquire targets abroad in order to attain access to better technology and overseas capital markets while also further developing the domestic economy.

[Insert Figure 1]

Figure 1 reports the twelve-month moving average for the acquirer's three-day cumulative abnormal returns from 2000 until 2009 and it can be seen that there is a spike around the 2002 Act of Mergers and Acquisitions of Listed Companies followed by a dip given the economic crash experienced in the Shanghai and Shenzhen stock exchanges in 2003. Additionally, following the RMB exchange-rate reform of 21<sup>st</sup> June 2005, further reinforcing the 1999 "Go Global" policy, firm acquisition performance experienced a marked improvement reaching a peak up to 2.5%. Chinese acquisitions are certainly improving over time in terms of executing financially rewarding transactions.

## 2.2. Existing Literature

Morck, Yeung and Zhao (2008) highlight the importance of addressing the idiosyncrasies of the Chinese market. Using a dataset of 1,381 companies listed on the Shanghai and Shenzhen stock exchanges, they document that over half of these firms are directly owned by the state while the remainder are ultimately controlled by the government through state-managed investment funds and state controlled enterprises. This characteristic makes Chinese firms completely different from the usual type of bidders typically seen in the US or the EU.

Given the governmental involvement in the economy within China, not only in its actual dynamics but through the ownership and control it exerts over the key economic players, it is not surprising that the government's "Go Global" policy has triggered a steady upward rise in the level of foreign acquisitions undertaken. Focussing on the motivation and performance of companies that acquire foreign targets, Doukas and Travlos (1988) posited that such a decision could signal to the market the firm's intention to exploit capital market distortions, particularly via arbitrage activity of institutional restrictions, capturing of informational externalities or indeed via capitalization of economies on a global scale. Their work sought to ascertain whether firms could meet an international diversification objective via a multinational network that can offer systematic advantages. The results showed that the value is limited if capital markets are integrated and indeed when the home market of the acquirer is efficient. Positive and significant returns for multinational firms acquiring a firm in an economy in which the firm currently did not operate proved support for the propositions of the *positive multinational network* hypothesis<sup>2</sup>. Indeed, given that the domestic Chinese

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<sup>2</sup> Doukas and Travlos (1988) found strong returns for a bidder following the completion of an acquisition in which the target company is located within a country in which the bidder has not previously operated within. We tried to include a similar



market could be considered to have not fully integrated into the global economy, such that therefore it possesses particular distortions such as the political censorship of information, going abroad at the firm-level could offer a way for domestic investors to globally diversify their position indirectly and exploit the faced capital market distortions.

Morek and Yeung (1991), taking inspiration from Doukas and Travlos (1988), examined three further key hypotheses regarding why firms move from a unination to multinational operation centered upon US firms. They firstly theorize that direct foreign investment occurs at times in which the firm itself is set to be able to extract value from global expansion of its valuable intangible assets, which includes factors such as patents, marketing abilities and so forth. The value of these intangible assets is theorized to be directly proportional to the degree of multinationality of the firm, labeled the *internalization* hypothesis. The second argument is centered upon foreign acquisitions being a solution for managers seeking the confines of the complex structure of a multinational firm to avoid agency monitoring. Finally, the paper offers that multinationality can offer firms a way to avoid taxation laws and potentially to the ability to source low-cost inputs. The results mainly support the internalization theory, and in fact, little support is found for the other hypotheses discussed.

Updating this seminal work, Gubbi et al. (2010) examine the Indian market. They emphasize that the scope of previous studies is somewhat limited due to the previous ‘norm’ whereby bidders typically originated within developed economies, acquiring those located in less developed countries. The crises engulfing Western nations undoubtedly offers an opportunity to examine the consequences and performance of the reverse situation – whereby an emerging market, fuelled by high foreign reserves and appreciating currencies, homes the initiating party. Gubbi et al. (2010) assess the value of the *reverse internalization* hypothesis, whereby the bidder acquires to buy the intangible assets of the target, rather than acquiring to spread the value of their own. Arguably this is a necessary update given that it is the intangibles of technology, patents, knowledge and other valuable resources that are held by the targets that are required to both project and enhance the competitiveness of domestic firms within the global economy, as well as to further propel the mainland’s ongoing economic development.

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dummy into our analysis but there were only 24 deals that represented the first move of the bidder into the target’s nation. The results of this analysis were insignificant, most probably due to the small sample, and so we could not reliably report the results. It does however serve as an opportunity for further research as Chinese FDI continues to increase year-on-year.

In a related study, Changqi and Ningling (2010) try to assess the true determinants of China's FDI. They hypothesize that a better pre-acquisition performance should produce better cross-border financial rewards in line with the Q-theory of mergers. A well-managed firm should enjoy a steady or upward stock price and thus those with better pre-merger performance should be those deemed to be well-managed firms that can transfer their superior leadership to the target. Moreover, because of state-ownership, many Chinese companies do not pay out dividends in order to keep control of the firms' funds (Changqi and Ningling, 2010; Morck, Yeung and Yu, 2008; Chen and Young, 2010; Sun and Tong, 2003). Although legislation has been established forcing firms to pay out a minimum of 20%, many would still opt to retain all earnings given the choice in order to preserve control. State-ownership can mean a lack of transparency between managerial decisions and the firm's shareholders (Wei, Xie and Zhang, 2005). This informational asymmetry can lead to negative announcement returns for firms engaging in foreign acquisitions. Shareholders are modeled as reacting to the governmental decision to direct such action, rather than to the quality of the deal itself. Changqi and Ningling (2010) also stress that an older firm will have more experience and thus there should be a positive relation between a firm's age and foreign acquisition returns, which may also explain the degree of influence that can be exerted by the state.

### 2.3. Hypotheses Development

Chinese foreign investments have amassed growing media coverage in the developed world (The Economist, 2011-12). A paradigm shift of power is invoking much interdisciplinary attention, specifically marrying together politics with finance (Jacques, 2012). Yet despite the mass of anecdotal evidence, there have been few empirical studies that have specifically focused upon Chinese FDI.

While many papers have focused on China's unique political structure (Gao and Kling, 2009; Xu et al., 2011; Wu et al., 2012; Zhou et al., 2012), none to our knowledge has investigated the financial performance of domestic acquisitions relative to foreign ones. China has been documented as having an increasing trend in both the level and scale of acquisitions. We've now had over ten years of acquisitions abroad and China has become an ideal testing ground for updating and refining the evidence regarding the value of multinationality. As the world's future superpower (Jacques, 2012), in-depth analysis is warranted both politically and

economically for China itself, as well as for those starting to begin to understand this traditionally opaque economy.

We focus our first hypothesis therefore upon the financial performance of domestic acquisitions relative to foreign ones to shed new light on the multinationality vs. uninationality debate. The seminal paper of Doukas and Travlos (1988: 1161) theorizes that multinational corporations can earn a stock price premium through the unique selling point of being able to transfer firms' resources on an international scale through a *globally maximizing network*. The study found supportive evidence of firms moving abroad, specifically into a "new" market whereby a firm that did not have any previous operations in that country was shown to be able to exploit profits from this new global exposure. Multinational corporations therefore advance their shareholders profits' when they move into a new market, via diversification of the proposition of the firm, as well as indirectly the portfolios of the investors that hold the firm's stock. This theory, denoted the *positive multinational network hypothesis*, promotes multinationality as a vehicle through which investors can diversify their positions, that individually they would be restricted from doing due to capital market distortions. Contextually, this appears particularly appropriate for Chinese investors that suffer from controlled currency flows, restricted and censored media as well as limited understanding of foreign economies.

Morck and Yeung (1991) furthered this work by critically evaluating three further motives for moving abroad – tax avoidance and low-cost inputs, managerial objectives and internalization. The *internalization* hypothesis conceives that FDI occurs at times when the multinational corporation possesses valuable intangible assets that it can enhance in value through international expansion of its operations. The ability to be able to control foreign operations *should* allow for profits, which will be theoretically limited only by the potential costs of managing the foreign subsidiary.

In a contemporary study using Indian data, Gubbi et al. (2010) emphasize that the internalization hypothesis can and should be updated to allow for the concept of inorganic growth via M&A activity – that is, for developing nations to leapfrog the conventional path of economic development via the foreign acquisition of both tangible and intangible assets. The acquisition of intangible knowledge, that would require time and patience to be grown organically, can be a lucrative strategic opportunity for emerging markets.

Applying this evidence to China it would anecdotally appear that such arguments have substance. The characteristics of the Chinese state documented are such that foreign acquisitions present a unique opportunity to shed additional light on the existing literary debate. With this in mind, we are led to the first testable proposition:

***H1: Foreign acquisitions generate positive abnormal returns for Chinese firms.***

Target selection is debatably the most important decision in the M&A process. Finding a target that can strategically enhance bidder value is imperative to ensure sufficient financial synergy both exists and can be extracted. An integral part of the motivation to move abroad, the industry and size of the target relative to the bidder could prove an important explanatory determinant of firm performance. Boateng et al. (2008) decompose the strategic motivation of Chinese acquirers within a sample of 27 foreign transactions that took place over the period 2000 to 2004. They find that foreign acquisitions tend to be economically motivated such that value is created through diversification, acquisition of foreign technology and faster entry into new economies. In related work, Gu and Reed (2010) explore the market reaction to 145 overseas M&As over a fourteen-year period from 1994 to 2008. Their work specifically focuses only on the effects of the “Go Global” policy of 1999 and finds supportive evidence that the market responds positively towards the announcement of M&As. They reason that the “Go Global” policy has allowed for domestic Chinese enterprises to seek profit-improving transactions, while they also note that the cross-border investment itself has directed more of China’s wealth towards profitable industries such as resource and technology. Conn et al. (2005) also report that foreign acquisitions of high-tech firms can extract merger profits due to the inherent synergy of effectively acquiring knowledge driving firm innovation.

The *reverse internalization hypothesis* posits that it is the very resources that the target offers relative to what the bidder possesses that motivates the firm to conduct a foreign acquisition. Spreading the operations of the company onto the international arena can be lucrative if there is an opportunity for the firm to strategically position itself in such a way that will propel the competitiveness of the product offering. Given the anecdotal media coverage of Chinese acquisitions (i.e. Lenovo-IBM; Geely-Volvo), it does appear that targets in resource-related

industries are particularly important from a political and economic standpoint (Gubbi et al., 2010). Given this evidence, we are led to our second testable proposition:

***H2: Foreign acquisitions of targets located in resource-related industries (e.g. energy, industrials, technology) will provide higher positive abnormal returns than those in other industries.***

### **3. Data and Methodology**

#### **3.1. Dataset**

We compile our Chinese merger dataset from Thomson One Banker SDC with share price and accounting information sourced from Thomson DataStream. Information related to specific deal characteristics (such as firm names, target nation, and so forth) are taken from Thomson One Banker SDC. The sample period studied is 01/01/2000-31/12/2009 due to the limited number of cross-border deals prior to the encouragement of the People's Republic of China in the "Go Global" policy of 1999. Furthermore, our sample ends in 2009 for the requirement of the availability of data in the long-run post-merger performance.

For a deal to be included in our sample, we required that it meet the following criteria:

- The acquirer must be listed on a Chinese stock exchange – either Shenzhen or Shanghai – with a valid DataStream code such that public financial information can be sourced.
- The deal must take place between 01/01/2000 and 31/12/2009.
- The deal must have a deal value greater than \$1 million to account for the relative size effect (Asquith et al., 1983).

The initial total sample size of the dataset satisfying these criteria is 1,400 deals. Due to a lack of data related to market value (MV), market-to-book value (MTBV) and payment method of the deals, 942 deals were removed such that the final sample size is comprised of 458 deals.

The focus of this paper is placed upon the performance of foreign acquirers relative to domestic ones. We therefore split our sample into two sub-groups – one in which the target

was domiciled outside of the Chinese stock market, and one where the target was domiciled in China. This splits the sample into 4,15 domestic Chinese deals and 43 cross-border ones.

[Insert Table 1]

Panel A of Table 1 reports the time distribution of deals for the final sample by year and deal value. We can see that there is a gradual increasing trend for the number of M&As completed since 2000 for both categories. In particular, following China's entry into the World Trade Organisation (WTO) in 2001, international expansions have become increasingly popular. Politically, the People's Republic of China has been encouraging Chinese investment abroad (Gartland, 2012) and this is shown to have grown by 500% from the period 2001 to 2010.

While the volume of these transactions is undoubtedly low as compared to perhaps a more developed M&A market such as the US, the economic value of these transactions is significant. The time distribution in our sample by deal value indicates that in 2001, international Chinese M&As were valued at \$0.021 billion. By 2008 this had increased to an astonishing \$5.054 billion<sup>3</sup>. Additionally, within 2008, the People's Republic of China introduced further regulation for overseas acquisitions within the financial sector as a result of the sub-prime crisis that had begun to cripple the global economy, to ensure this money is well spent abroad. This regulation defines that any ownership of 20% or more within a foreign institution by a Chinese company should be classified as a "significant holding" while it was also specified that Chinese overseas acquirers would be restricted from buying into any foreign company that had suffered either significant losses or a low employee retention ratio (Comtex News Network, 2008). It is clear that China is focused on trying to develop a success strategy for overseas M&A's to contribute to, and not detract from, the development of the Chinese domestic economy.

The political encouragement to invest abroad is undoubtedly seeping into the investment decisions of Chinese firms. While it is evident that cross-border deals are a key initiative of the government, domestic deals are also on the rise. Panel A of Table 1 indicates a significant increase in the volume and value of domestic M&As as well, particularly since the creation of

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<sup>3</sup> Comtex News Network documented that by September of 2008, foreign M&As had surged by 49.8% overall totaling more than \$17.6 billion. Due to the availability of data and non-listing of some of these acquirers, we can't include all within the sample studied within this paper. Nevertheless, leading banks such as Bank of China, China Construction Bank, Bank of Communications and Guangdong Development Bank were shown to be conducting some of the more significant deals.

the 25-member M&A committee in 2008, solely tasked with ensuring that any merger, acquisition or restructuring plan is examined intensely so as to provide support for listed companies that decide to consolidate their assets domestically with similar firms (Agence France Presse, 2008). The target nation is shown in Panel B of Table 1 to largely be within Hong Kong, which accounts for circa 50% of the foreign sample. This is unsurprising given the conveyance of Hong Kong from British to Chinese sovereignty in 1997.

Media coverage and existing literature from the Western world (Gu and Reed, 2010; Boateng et al., 2008) regarding Chinese acquisitions has noted acquirer's sector preferences. Panel C of Table 1 reports the time distribution of targets stratified by industry. It can be seen that there is a strong preference for targets to be listed in resource-related sectors, particularly in the foreign sample. Domestic acquirers appear to acquire firms within the industrials, materials and hi-tech sectors. This is also true for foreign acquisitions. Anecdotal evidence has covered the debate between China's transactions moving control of scarce resources towards the East. Our evidence supports that there is a preference for targets within resource-related sectors for both domestic and foreign transactions.

While the People's Republic of China has taken numerous measures to encourage M&A activity, be it domestically or internationally, the question remains whether or not these deals are generating value for the acquiring firms. This paper fills this void and the methodological approaches followed are now presented.

### 3.2. Methodological Approaches

This paper investigates the performance of domestic and foreign acquisitions undertaken by listed firms in China. As outlined in the previous section, the full sample is split into two sub-samples – one that includes acquisitions of domestic Chinese targets ('Domestic') and the other that includes acquisitions of foreign targets ('Foreign').

In addition, we note the abundant literature that highlights the need to control for the size of the acquirer (Moeller, Schlingemann and Stulz, 2004). For this reason, we create secondary portfolios stratifying each sub-sample according to acquirer size, as measured by the firm's MV two months prior to the acquisition. The firms are then sorted according to their size,

where the top one third is classified as ‘Large Acquirers’ and the bottom one third is classified as ‘Small Acquirers’<sup>4</sup>.

The performance of all portfolios of acquiring firms is measured in terms of both the short-run and long-run abnormal return’s (AR) generated by the M&A deal. The short-run analysis centres on a three-day event window (-1, +1) employing the Market Adjusted Abnormal Return approach (Seiler 2004; Brown and Warner, 1980; 1985) whilst the long-run share-price affects are assessed using the size-adjusted Buy-and-Hold Abnormal Return (BHAR) approach of Lyon, Barber and Tsai (1999) and Bouwman, Fuller and Nain (2009). The analyses aim to identify what the short-run market reactions were for acquiring firms, defined as the abnormal returns generated by the deal announcement. Moreover, the work then progresses to determine whether the short-run ARs transpire into long-run acquirer value.

### 3.2.1. Short Term Analysis

The short-run analysis is conducted as an event-study over a three-day announcement window (-1, +1)<sup>5</sup>. We calculate the normal returns of the firm using daily price data as follows:

$$R_i = \ln\left(\frac{P_t}{P_{t-1}}\right) \quad (1)$$

Where  $R_i$  relates to the daily normal return of stock  $i$  while  $P_t$  and  $P_{t-1}$  refer to the stock price on day  $t$  and  $t - 1$  respectively.

In determining the short-run announcement effects, we note the abundant methods available (Sharpe, 1964; Lintner, 1965; Lyon et al., 1999; Brown and Warner, 1985). Due to the restrictions of models such as the CAPM (Roll, 1977), we follow the guidelines of Seiler (2004) and define abnormal returns as being anything earned by the firm that exceeds the systematic market compensation each day, such that the expected return of a stock is assumed to be the return earned by the market (Seiler, 2004: 220). This market adjusted AR approach

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<sup>4</sup> We also use a 15% and 20% cutoff level within robustness tests and the results are found to be consistent with our main findings.

<sup>5</sup> We also use (-2, +2) event window on the M&A announcement date within robustness tests and find the results to remain consistent with our main findings.



is in line with Brown and Warner (1980; 1985) so that AR's are defined as the excess stock return earned by the firm adjusted for the market over the sample period (Buchheim *et al.*, 2001: 22). The normal stock returns ( $R_{it}$ ) must have the normal market return ( $R_{mt}$ ) deducted in order to generate the AR for each of the three days as follows:

$$AR_{it} = R_{it} - R_{mt} \quad (2)$$

Where  $R_{mt} = \ln\left(\frac{P_t}{P_{t-1}}\right)$ .  $R_{mt}$  is the normal market return calculated using the daily price of the Shanghai Stock Exchange over the sample period. The AR's are then summated to give the Cumulative AR (CAR) for each firm as follows:

$$CAR_{it} = \sum_{i=0}^n AR_{it} \quad (3)$$

This short-run univariate analysis will involve the above process for each portfolio. The portfolio t-statistics are computed using the formula:

$$t = \frac{AR_T}{\sigma(AR_T)/\sqrt{n}} \quad (4)$$

Where  $AR_T$  refers to the sample mean, and  $\sigma(AR_T)$  is the cross-sectional sample standard deviation for the sample of  $n$  firms.

### 3.2.2. Long Term Analysis

In assessing long-term acquirer share price effects, Fama (1998) claims that the use of different methodological approaches in empirical research will lead to different conclusions being drawn such that the testing process itself, in effect, becomes a one over the choice of econometric model to use rather than a direct test of the study at hand. He further stresses that the assessment of various events using different models could often lead to eradication of the existence of an anomaly. As a consequence, choosing the correct model is therefore imperative.

To combat problems associated with long-run analysis and the noted bad-model problem (Fama, 1998), we employ the use of the twenty-four month Buy-and-Hold Abnormal Return (BHAR) approach. While the Calendar-Time Portfolio approach (CTPA) is a worthy alternative, upon its implementation we encountered a number of problems with the size of some of the portfolios due to a smaller number of deals within them and there was a question over our ability to reliably interpret such sample results. In this way, the long-run price effects are analysed in terms of the favoured BHAR approach of Loughran and Vijh (1997) and Buchheim et al. (2001).

Size-adjusted twenty-four month BHARs are calculated following the methodological framework of Lyon, Barber and Tsai (1999), and Bouwman, Fuller and Nain (2009). Specifically, size-adjusted abnormal returns are calculated as follows:

$$BHAR_{it} = \prod_{t=0}^T (1 + R_{it}) - 1 - R_{pt} \quad (5)$$

where  $R_{pt}$  relates to the reference portfolio return, calculated as follows:

$$R_{pt} = \sum_{j=1}^n \frac{\prod_{t=0}^T (1 + R_{jt}) - 1}{n} \quad (6)$$

where  $R_{jt}$  is the simple return on firm  $j$  at time  $t$  and  $n$  is the number of firms.

In each year, there are 50 reference portfolios (in terms of size and market-to-book). The reference portfolios are created in two stages following Bouwman, Fuller and Nain (2009). First, in June of each year  $t$  from 2000 to 2009, we rank all Chinese firms listed in the Shanghai and Shenzhen Stock Exchanges on the basis of their MV. Size deciles are then created on the basis of these rankings. Second, within each size decile, firms are sorted into quintiles based on their market-to-book ratios (MTBV) in December year  $t-1$ . We then drop firms with negative MTBV when calculating MTBV breakpoints<sup>6</sup>.

The BHAR approach itself is well used within recent literature and is the advocated method for long-term return analysis (Lyon et al., 1999). Lyon et al. (1999) indicate that the BHAR method provides an accurate measure of the AR's experienced by an investor. However,

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<sup>6</sup> We also calculated 12 month and 36 month BHARs for our sample in robustness tests and the results remain consistent with our main findings.

Fama (1998) posits that long-run BHAR's suffer from compounding expected-returns. Furthermore, BHAR's can produce a statistically significant result even when none is present due to the effect of short-run movements (Buchheim *et al.*, 2001: 28). The possible positive-skewness problem can yield potentially misleading results and thus may cast doubt over the efficiency of the output generated from statistical analysis.

Therefore, we employ the use of a bootstrapped t-statistic as well as using the non-parametric Wilcoxon rank-sum test for estimating the differentials. These statistical methods have gained prominence within the literature as research has begun to criticise the potential skewed-distribution problem of the BHAR approach (Barber and Lyon, 1997). BHAR's do accurately reflect the effect of a particular corporate event upon the investor and their holdings (Buchheim *et al.*, 2001: 28) and it is for this reason that they are utilized for assessing the robustness of the long-run performance of Chinese acquirers.

### 3.3. Robustness Tests

In order to ensure the reliability of the results produced, robustness checks for the short and long-run are also conducted. The short-run window has been expanded from three-days to five-days to further assess the financial announcement impact. The three-day CAR's results are reported but it worth noting that we also find the results from a five-day event window to be very similar. Finally, the long-run window is also calculated for twelve months and thirty-six months separately. Once again, we find that the results largely support our main findings although some coefficients lose their significance. For brevity these results are not reported but are available upon request.

### 3.4. Multivariate Analysis

In addition to the univariate analyses, a multivariate examination is specified so as to examine those variables that can help explain the variation in acquiring firm's returns. As criticized by Draper and Paudyal (2008), the univariate analysis fails to allow for the interaction of alternative variables upon acquirer's gains, and consequently we extend our analysis to model such interactions. The three-day CAR's (twenty-four month BHARs) at the date of announcement are investigated in the following multivariate framework:

$$CAR_{(-1,+1)} = \alpha + \sum_{i=1}^N \beta_i X_i + \varepsilon_i \quad (7)$$

$$BHAR_{(+1,+24)} = \alpha + \sum_{i=1}^N \beta_i X_i + \varepsilon_i \quad (8)$$

In equations seven and eight, the constant reflects ‘*everything after controlling for the effects of all the explanatory variables*’ (Draper and Paudyal, 2008: 395). We follow a winsorization process whereby all continuous variables are winsorized at 1% and 99% to minimize the influence of outliers. In this setting, we include a vector of explanatory variables,  $X_i$ . The main variable to be assessed relates to whether or not the target is Chinese. Therefore, we include a dummy variable, which takes the value of one if the target is located outside of China, labeled as ‘**Foreign**’. Furthermore, when examining the performance of Chinese acquirers, it is necessary to control for the ownership status of the firm. The People’s Republic of China is strongly involved with the dynamics of the Chinese economy. Decisions to acquire abroad must pass through the state controls system, put in place to prevent any acquisitions of distressed international firms, which could cause financial difficulties for the acquirer. Furthermore, those firms that are owned by the government (State Owned Enterprises [SOE]), which proceed to perform domestic M&A’s, must also take guidance from the 25-member M&A committee. Chinese M&A legislation and government involvement for SOE firms means that the decision to merge could be considered more of a political rather than economic act. Additionally, recent research has shown there to be a positive influence attached to the performance firms that have state ownership within the Chinese economy (Zhou et al., 2012). For this reason, we include a dummy variable labeled ‘**SOE Bidder**’ that takes the value of one if the bidder is a SOE.

In addition, we include a series of control variables known within the literature to have a significant impact on the returns of the acquirer. Firstly, Asquith, Bruner and Mullins (1983) find that the size of the target relative to the acquirer can help explain a significant proportion of acquiring firm returns surrounding a merger. The premise behind this proposition is that the smaller a target is relative to a bidder, the lower the impact that will be felt in the bidder’s operations subsequently leading to a lower stock price impact. We control for this relative size difference between the bidder and the target by scaling the value of the deal relative to the acquiring firm’s market value, measured two months prior to the merger announcement date. This variable is included in the regressions and labeled ‘**Relative Size**’.

Travlos (1987) also writes that the use of equity in the payment method of M&A deals signals to the market that the acquirer is overvalued while full-cash payment would indicate potential undervaluation of the acquirer, both proposed under the asymmetric information framework of Myers and Majluf (1984). We therefore include two payment method dummy variables. The first is labeled '**Stock**' and this variable takes the value of one if the bidder uses 100% equity to buy the target firm. In addition, we include a secondary payment method variable labeled '**Cash**' which takes the value of one if the bidder uses 100% cash financing to pay for the target.

Recent literature emanating from the field of behavioral finance has also highlighted the importance of the valuation of the market at the time of the merger announcement. Rhodes-Kropf and Viswanathan (2004), and Shleifer and Vishny (2003) highlight the importance of the stock market in the M&A process. Rhodes-Kropf and Viswanathan (2004) show that merger activity is significantly correlated with high market valuations. Shleifer and Vishny (2003) additionally argue that it is the stock-market which drives acquisitions through creating incentives to issue and use overvalued equity to purchase target firm assets. Finally Bouwman, Fuller and Nain (2009) find evidence that indicates mergers conducted when the market is valued highly result in high announcement returns but poor long-term performance while the reverse is found for those conducted in low-valuation markets, suggesting that the quality of mergers is influenced by the valuation of the market at the time of deal announcement. Taking heed of this evidence, we control for the valuation of the market following the methodology of Bouwman, Fuller and Nain (2009) whereby we detrend the price-to-earnings (PE) ratio of the Shanghai Stock exchange<sup>7</sup> and classify the largest 25% PE corresponding months as being highly valued and the smallest 25% PE corresponding months as being valued low. Deals conducted in a high-valuation month take the value of one in a dummy variable labeled '**High-Valuation Market**' while those that are conducted in a low-valuation month take the value of one in a dummy variable labeled '**Low-Valuation Market**'.

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<sup>7</sup> Since the Shanghai Stock Exchange does not directly report the P/E, we calculate the average P/E of all shares listed on the Shanghai Stock Exchange. The top and bottom 0.5% of observations (i.e. outliers) are removed in calculation. Subsequently, we de-trend the P/E in accordance with Bouwman, Fuller and Nain (2009).

In a similar vein, related literature in the field of IPOs highlights the interrelationship between the states of the economic cycle with the activities of firms within it. In work conducted by Yung, Colak and Wang (2008), firms are influenced by whether the market is “hot” or “cold” in terms of the level of IPOs undertaken. We take note of this research and agree that the level of acquisitions within an economy at one period in time could plausibly impact the firm’s decision to acquire. Thus, we control for the impact of the level of corporate activity in the economy, specifically in relation to the number of M&As being undertaken. To measure the level of activity within the M&A market, we initially follow the method of Yung, Colak, and Wang (2008). Specifically, we compare the moving average with the historical average of the M&A activity in all previous quarters going back to 1995. However, since there are only a few deals before 2000, the moving average is always 50% (also true for a 60% cut-off) above the historical average. In other words, according to this method, nearly all the quarters are define as “hot” for China’s M&A market because of the growing trend. Therefore, we use another method to identify the M&A market heat. Adapting the intuition of Bouwman, Fuller and Nain (2009), we classify a quarter as “hot” (“cold”) if the number of M&A deals in the quarter is 10% above (below) the average number of deals over a two year window around the quarter (i.e. one year before to one year after the quarter). We then create a continuous variable labeled ‘**Market Heat**’, which is calculated as the moving average of the number of M&As announced in each quarter divided by the historic average of the M&As announced in all previous quarters spanning back until the onset of the sample period.

It is also worth controlling for the currency appreciation experienced in the Chinese RMB. The People’s Republic of China exerts strict control via the State Administration of Foreign Exchange (SAFE) over foreign exchange transactions such that the domestic currency is not freely convertible in international currency markets (Junnan and Yun, 2012). The tight control has been increasingly loosened over the past decade and looks set to continue in the same fashion. In this decade, the RMB has appreciated considerably and analysts are forecasting it will continue in the same fashion in the forthcoming years, with HSBC approved as the Chinese central bank’s market maker for direct trading of Chinese yuan and Japanese yen. We believe that the appreciation of the Chinese currency could also help explain the performance of acquiring firms in that if the firm is able to acquire cheaply abroad then this could work to the benefit of shareholders. For this reason, we include a variable that measures the appreciation of the Chinese currency relative to the global

benchmark of the US dollar, labeled '**Currency Appreciation**'. This dummy variable takes the value of one if the deal is conducted after the RMB exchange rate reform of 21<sup>st</sup> July 2005.

We also include additional standard control variables such as the logarithm of the MV of the bidder (labeled '**LN(MV)**') measured eight-weeks before the deal announcement to control for size effects; the MTBV (labeled '**MTBV**') of the bidder measured eight-weeks before the deal announcement to control for valuation effects; the listing status of the target, which takes the value of one if the target was a publicly listed company, labeled '**Public Target**'; the experience of the bidder in mergers and acquisitions such that if the bidder has performed 3 or more mergers before the acquisition in question, then they are classified as an experienced bidder, labeled '**Experienced Bidder**'; the run-up of the stock performance of the acquirer in the year before the announcement date over a window of (-364, -7), labeled '**RUNUP**'; as well as finally, the industry of the target, which takes the value of one if the target is situated in an industry other than that of the bidder, labeled '**Diversifying**'.

### 3.5. Summary Statistics

[Insert Table 2]

Table 2 presents the summary statistics of both domestic and foreign acquisitions. Instantly, it can be seen that despite the volume of foreign deals in the sample being only 10% that of domestic ones as shown earlier also within Table 1C, the size of the target is considerably larger as measured by the MV of the acquirer eight-weeks before the announcement date. Thus despite foreign transactions being low in volume terms, the size of these transactions is economically significant. On average, acquirers of domestic Chinese targets have a market value of \$1.2 billion while foreign acquirers have a mean MV of a staggering \$22.74 billion. As a result, the relative size of the transactions is shown to be larger for domestic deals given the smaller average size of acquirers of domestic targets.

Furthermore, the MTBV of foreign acquirers is shown to be much lower than that of domestic acquirers. Foreign acquirers have a MTBV of 2.83 while domestic ones have an extremely high value of 6.36. According to the existing literature, this infers that foreign acquirers have valuations typically closer to their fundamental level than those undertaking

M&A within Chinese borders. This is not surprising given the stringent controls SAFE places on foreign exchange as well as the M&A committee, in place to help encourage the success of international expansion.

As noted earlier, the ownership status of Chinese firms is believed to be a significant factor influencing the returns of acquiring firms (Zhou et al., 2012). The summary statistics show that 144 targets of domestic acquirers are SOE firms. This provides support for the documented evidence that the People's Republic of China is actively encouraging consolidation of domestic assets so as to improve the efficiency of the economy.

Table 2 also shows that there is a high preference for cash financing in both sub-samples examined. 57% of domestic deals and 70% of foreign ones are paid for with 100% cash. The stronger preference for cash in international acquisitions is not surprising given the controlled nature of the Chinese domestic economy. The government has tight controls not only over the outflow of money from the economy but also over the inflow of investment. Furthermore, many Chinese companies as well as the government itself have built large cash reserves that are ripe for international investment. It was reported in 2009 that the state in Beijing had diverted \$1.95trillion towards encouraging overseas oil investments (National Post's Financial Port & FP Investing, 2009).

We additionally include noted statistics from the existing literature, in particular the run-up of the acquirer's stock performance prior to the announcement of the deal. It is plausible to suggest that there is information leakage around domestic transactions rather than cross-border ones, given the higher level of information regarding both parties in domestic deals. The run-up variable indicates that there is a 5.94% increase in the acquirer's stock price in the year before the acquisition rather for those purchasing domestic targets. Conversely, foreign acquirers experience a poor economic performance in the one-year prior to the acquisition with a -19.62% decline in their stock price. Acquiring abroad could possibly be motivated by a desire to improve the offering of the firm beyond that of the domestic economy.

When we examine the announcement effect, we can see that the Chinese economy reacts much better towards acquisitions of domestic targets rather than foreign ones. Domestic acquirers see a 2.76% return on average when announcing their deal, whereas foreign acquirers experience losses of -0.58%. However, interestingly, while the market does not



respond well in the short-run, over the long-run it is shown that foreign acquisitions generate a 14.2% BHAR, relative to the long term losses of -7.98% generated by domestic acquirers. It is worth mentioning at this early stage that China's heightened attention on ensuring foreign acquisitions provide benefits for the domestic economy do indeed lead to positive long-run market reactions.

While the summary statistics indicate that we have included correctly all necessary controls, it is necessary for us to look in more depth at the performance of the portfolios under analysis – categorized according to size and value. The empirical results of this work will now be presented.

## **4. Empirical Results**

### **4.1. Short-Run Analysis**

Earlier in the work, we stated that the primary aim of this work is to examine the performance of foreign acquisitions relative to domestic ones. In our first hypothesis, we proposed that foreign acquisitions should outperform domestic ones given the results of the previous empirical evidence (Doukas and Travlos, 1987; Morck and Yeung, 1991; Moeller and Schlingemann, 2005; Conn et al., 2005; Chen and Young, 2010; Gubbi et al., 2010). Table 3 reports the short-run performance for the full samples.

[Insert Table 3]

The results indicate that over a three-day event window, domestic acquisitions earn 2.76% (0.000) significant announcement returns. These positive returns hold regardless of the method of payment used. Cash acquirers earn 1.30% (0.000) announcement returns while equity is very positively received in the Chinese economy with 6.24% (0.000) bidding firm returns. This is in contrast to the evidence from the West, where stock acquisitions result in negative market reactions due to asymmetric information (Travlos, 1987).

However, foreign acquisitions lose -0.58% (0.604), statistically insignificant at any conventional level. The returns remain insignificant when stratified according to method of payment. Despite these insignificant announcement returns, the two-sample t-test between the

two groups shows that domestic acquisitions statistically outperform foreign ones by 2.45% (0.006) on average refuting our first hypothesis that Chinese firms that acquire overseas earn better abnormal returns. The results of Table 3 indicate that acquisitions of domestic targets results in statistically significant higher announcement returns than those of foreign targets.

Previous studies have found that the size of the acquirer is shown to have a significant impact on the performance of acquiring firms, where small acquirers should outperform large ones (Fama and French, 1992; Moeller, Schlingemann and Stulz, 2004). Panel B of Table 3 reports the returns for small domestic and foreign acquirers. The results indicate that size plays an insignificant role in the returns to foreign acquisitions in the short-term. On average, small foreign acquirers lose -0.36% (0.853) around the announcement date, statistically insignificant. In contrast, small acquirers of domestic targets realize significant gains of 3.58% (0.000) at the announcement, increasing to a significant 8.27% (0.003) when the deal is equity-financed. 21.58% of deals conducted by small domestic acquirers are financed with pure-equity whereas 50.36% are financed solely using cash. Despite the previous literature suggesting that the use of equity signals overvaluation of the bidder (Travlos, 1987), the Chinese economy does not receive such a signal and the use of equity, even in its small percentage, generates significantly high market returns. This suggests that the Chinese economy welcomes equity transactions of small firms. Again, the domestic sample outperforms the foreign one significantly by 3.93% (0.071) when the acquirer is classified as small, insinuating that smaller firms would reap better short-term price reactions by acquiring domestically.

The results of Panel's C and D indicate that these returns are significantly lower for large acquirers. Panel C of Table 3 shows the performance of large acquirers around the announcement of their deals, while Panel D conducts a two-sample statistical analysis between small versus large firms. There is no statistical difference between small and large acquirers in the short-run for either domestic or foreign acquirers as evidenced in Panel D.

An interesting characteristic is the reaction to equity transactions. The existing literature related to firm size implies that small firms exhibit higher returns, and stronger price momentum relative to larger firms (Hong and Stein, 1997; Hong, Lim and Stein, 1998). One plausible reason is that small firms have a lower analyst coverage, which leads to a lag in the impounding of new information into their stock prices. Equally, alternative authors argue that

the root cause is the absence of liquidity in such firm, and barriers to arbitrage. While disagreement over the story behind this phenomenon continues on, the results are consistent in that small firms generate higher returns in Table 3.

If we apply some of this line of thinking to merging firms, then smaller firms could plausibly see higher returns as the market does not have full information related to the firm, or is simply not following the firm enough to react quickly to its news announcements. This could arguably lead to a higher performance of equity-financed deals relative to larger acquirers. On the other hand, for large firms, the story would imply the opposite – there should be more market attention placed towards these firms, such that, in line with the previous literature, the signal of overvaluation emanating from the use of 100% equity should generate a downward market correction. Large firms should have lower barriers to arbitrage arguably and therefore their prices should be more in line with fundamentals. This is the intuition behind most Western findings. However, for large Chinese acquirers using equity there is a statistically significant positive market reaction of 5.13% (0.002). While it is recognized that only 17.69% of large acquirers finance their deal using 100% equity, we still note the result to be a unique finding of the Chinese M&A corporate control arena. Yet we find insignificant announcement returns in the foreign sample for large firms. Furthermore, the sample disintegrates to virtually nothing when the method of payment is controlled for, with 90.48% of deals being financed using solely cash.

Earlier, in the summary statistics (Table 2) we found that there is a preference for Chinese acquirers to purchase targets operating in resource-related sectors and this formed our second hypothesis. Table 4 presents acquirer performance based on the industry of the target.

[Insert Table 4]

The results show that those firms acquiring within resource-related sectors generate significantly positive returns, particularly for domestic transactions. Acquirers of energy targets earn 3.78% (0.005) on average while also gaining 3.25% (0.000) if purchasing firms within the industrial sectors. It does appear however that these transactions are largely driven by the domestic sample especially given the smaller number of observations for the foreign one. Nevertheless, the choice of target industry is shown to be an important decision for Chinese acquirers to create shareholder value.

## 4.2. Long-Run Analysis

The existing literature has highlighted the long-run underperformance of merging firms. Table 5 reports the long-term performance of Chinese bidders controlling for firm size over a twenty-four month holding period post-merger announcement.

[Insert Table 5]

The results of Table 5, Panel A indicate that overall, domestic acquisitions generate statistically significant long-term wealth losses of -7.98% (0.023) while foreign acquisitions generate insignificant returns of 14.20% (0.656). This performance for both samples is consistent for cash and mixed-method payments. However, while equity-financed domestic acquisitions earn significantly positive short-term returns, the market does not correct this positive upward price over the long-term. There are positive but insignificant returns for these companies. In relation to our first hypothesis, foreign acquisitions significantly underperform domestic ones when using cash by -18.01% (0.041).

After controlling for firm size in Panels B (small acquirers) and C (large acquirers), the results show that small domestic acquirers have a much higher loss than larger ones - but this is statistically insignificant. In particular, cash-financed acquirers face losses of -20.98% (0.051) on average. For foreign acquisitions, Panel C reports that large firms generate long-term wealth gains of 22.39% (0.014), while this increases to 25.33% (0.001) when the payment method is constrained to 100% cash (which represents 90.48% of the large cross-border acquirer sample). This superior performance is also shown to be 29.81% (0.006) significantly higher than the performance of domestic large acquirers. This is the first result that supports our first hypothesis, indicating a financial benefit for Chinese firms of “going-out” of the domestic market and is consistent with the reverse internalization view. Overall, the evidence in Table 5 suggests that large Chinese firms that “go-out” can generate significantly higher long-run returns relative to those which “stay-in”, so long as the firm is economically large.

[Insert Table 6]

While large firms can benefit from acquiring abroad over the long-term according to the size of the acquirer, the industry of the target is shown to lose its explanatory power in the twenty-four months after the completion of the deal. Instead of the significant returns for acquirers of targets in resource-related sectors as in the short-run results of Table 4, Table 6 indicates that there are marginally significant losses for bidders of targets in the industrials sector to the level of -15.37% (0.061), while others show no statistical difference, but this is again driven by the domestic sample. This infers that the choice of target industry is not an explanatory factor for long-term value creation.

Overall, the long-term results indicate that foreign acquisitions generate significant wealth gains if the acquiring company is large. The summary statistics showed earlier that foreign acquirers are significantly larger than their domestic counterparts while anecdotal evidence from the nineties noted that the Chinese economy went through a large period of domestic restructuring and consolidation (Ma and Hurd, 2005). This seems to have produced certain profits for these respective acquirers over the long-term.

#### 4.3. Multivariate Analysis

While the univariate results have indicated that foreign acquisitions generate value only in the long-term for large firms, it is important to assess the cross-sectional relationships between the returns generated for acquiring Chinese firms and various known determinants highlighted within the existing literature. Earlier, in Section 3.1.4, we discussed the key variables to be assessed. These included various dummy variables to examine their influence on the performance of acquiring firms, defined according to key characteristics of the deals, such as whether the deal was foreign, whether the bidder had state-ownership and so forth. Table 7 presents the results of the short-term multivariate analysis.

[Insert Table 7]

Models 1 to 3 of Table 7 show that there is a significant negative relation between the performance of the acquiring company and the dummy variable **Foreign** – which measures whether the target is domiciled outside of the Chinese economy. This adds a different dimension to the univariate findings, which largely indicated that foreign acquirers generated a statistically insignificant market reaction. Here, the results strongly indicate at the 5% level

of significance that the market reacts negatively to announcements of foreign acquisitions. Furthermore, this finding holds across all specifications reinforcing the significance of the relation. The results indicate that the Chinese economy is not welcoming of foreign acquisitions in the short-term period.

In terms of the ownership status of the bidder, the results indicate that announcements of M&A deals by state owned firms, as measured in the dummy variable **SOE Bidder**, are positively received but this lacks statistical significance.

One of the most interesting results of the paper has been the positive market returns afforded to Chinese bidders which use equity as the deal's payment method. The univariate results indicated that Chinese acquirers that paid for their deal using 100% equity generated positive market reactions up to 8.27% (0.003) as shown in Table 3. The multivariate analysis however does not confirm this positive effect in the short-term period. Models 1 and 2 indicate that the use of 100% equity – as measured using the dummy variable **Stock** – leads to a insignificant positive market performance, while model 3 shows that the use of 100% cash – as measured using the dummy variable **Cash** – leads to a significantly negative acquiring firm return. This is in complete contrast to the US evidence, where the results found are the reverse – with stock financing being met with a negative market reaction due to the signaling of upward misvaluation.

We include an additional number of control variables noted within the literature within our cross-sectional analyses. Yung, Colak and Wang (2008) highlighted the importance of controlling for the level of corporate activity within the chosen field. For this work, we took their recommendation, controlling for the level of activity within the M&A market. The results in Table 7 indicate that there is no statistical impact of the level of M&As within the economy upon an acquirer's stock performance. The variable **Market Heat** is shown to be statistically insignificant across all models in Table 7 indicating that there is no effect on an acquirer's performance within China by the macroeconomic level of M&As being initiated.

While the level of M&A activity does not hold any explanatory power, the control variable **Leverage** indicates a statistically significant negative relationship. Ghosh and Jain (2000) find for the US that an increase in leverage around the merger announcement has a statistically positive impact upon the announcement period's market-adjusted returns. Table

7, however, indicates the reverse for the Chinese economy - the higher a firm's level of debt relative to total capital, the worse the performance of the acquirer. The Chinese economy therefore is shown to dislike acquisitions from levered firms.

[Insert Table 8]

When we move to look at the impact of these variables in the long-term within Table 8, we find that the significance of these relationships changes over time. **Foreign** loses its significance across all models. Moreover, in model 1, **Cash** has a significantly positive effect. Table 8 also shows that the variables **SOE Bidder**, **Relative Size** and **Stock** exert a significantly positive influence on the performance of the acquiring firm in the twenty-four months post-merger announcement.

While the size variable **LN(MV)** showed no significant effect over the short-term, the long-term cross-sectional analysis indicates that there is a positive relation with the performance of the bidder. This indicates that the larger a firm is, the better it will perform in the long-run post-merger performance, in line with the superior returns found for large firms over the long-run period within the univariate analysis.

In the long-run analysis of Table 8, we find that two additional control variables have a significant effect on the acquiring firm's performance. The listing status of the target is shown in models 2 and 3 to have a positive and statistically significant impact when publicly listed across all models within the dummy variable **Public Target**. Furthermore, the variable **Experienced Bidder** is shown to have a statistically significant effect on the performance of acquiring company's in the long-term period, across all models at a marginal significance level of 10%. This indicates that the more experienced a bidder is, the worse the long-term performance of the firm.

## 5. Concluding Remarks

This paper investigates the performance of acquirers acquiring domestically relative to those that acquire abroad, specifically following the encouragement of the 1999 People's Republic of China "Go Global" policy.

The results indicate that Chinese firms receive a better short-term market reaction when acquiring domestically with significantly positive returns while the cross-sectional regression analysis indicates that foreign deals negatively impact short-term returns. The results also show that larger a firm, the better its long-term performance, particularly when investing abroad. The results indicate that this consolidation and growth of Chinese multinationals is significantly improving the performance of foreign acquirers. Furthermore, those firms acquiring resource-related targets earn significant short-term profits around the announcement date but Western political concerns are at this stage unfounded given the low volume of currently completed foreign transactions.

This work renders many further research opportunities in relation to cross-border transactions originating from China. In particular, we recommend research centered on areas highlighted for growth by the Chinese government, specifically acquisition's within the energy and basic materials sectors. These undoubtedly will have long-term global effects, and research into the performance and efficiency of Chinese management of these scarce global resources is of undoubted economic interest. Finally, the political influence within these foreign transactions is irrefutably significant. We recommend that research into the political connections of these firms with the governments of foreign target is an interesting research field, open for further investigation.



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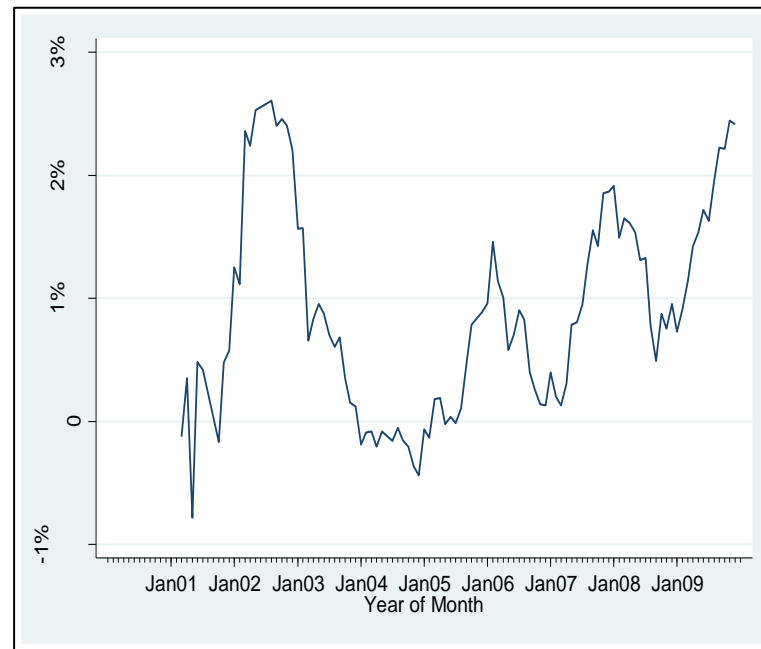
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**Figure 1: 12-Month Moving Averages**

This figure reports the twelve-month moving average of acquirer market-adjusted three-day cumulative announcement abnormal returns (CARs) for the full sample over the period 01/01/2000-31/12/2009. The full sample includes all completed deals that have bidder price data available on DataStream. The data requirements yield 1,055 observations. Extreme outliers (the largest and smallest 1% values) are omitted from the sample. The final sample includes 1,009 observations.



Note: The moving average of CARs reached its low around the RMB exchange rate reform of 2005, dated 21<sup>st</sup> July 2005.

**Table 1: Time Distribution of Deals**

This table reports the time-series distribution of the full sample. The domestic sample contains those deals where the target was a Chinese firm (Domestic) while the foreign sample relates to those deals where the target was located outside of China (Foreign). The figures shown represent the number of deals conducted within each category by year. All relates to the full sample studied. The Cash (Stock) sample contains those deals that are financed with 100% cash (stock). The Mixed sample contains the remaining deals that are financed using a mixture of cash and equity. Panel A reports the time distribution of the full sample by year (N) and deal value (Value), as measured in billions of dollars. Panel B reports the time-series distribution of deals by target nation for the cross-border sample. The figures shown in Panel B represent the number of acquisitions of targets from each nation by year. The countries are abbreviated as follows: Australia (AU); Canada (CA); Switzerland (CH); France (FR); Hong Kong (HK); Indonesia (ID); Japan (JP); Macau (MO); Netherlands (NL); Singapore (SG); Thailand (TH); Taiwan (TW); and United States (US). Finally, Panel C reports the time-series distribution of deals for the full sample stratified by the target industry. Panels C(i) and C(ii) refer to domestic and cross-border deals respectively. The figures shown in Panel C represent the number of acquisitions of targets within each sector by year. The industries are abbreviated as follows: CPS – Consumer Products and Services; CS – Consumer Staples; ENERGY – Energy and Power; FIN - Financials; GOVT – Government and Agencies; HEALTH – Healthcare; HI-TECH – High Technology; IND – Industrials; MAT – Materials; ENT – Media and Entertainment; PROP – Real Estate; RETAIL – Retail; and TELE – Telecommunications.

Panel A: Time Distribution of Deals by Volume and Value																
Year	All				Cash				Stock				Mix			
	Domestic		Foreign		Domestic		Foreign		Domestic		Foreign		Domestic		Foreign	
	N	Value	N	Value	N	Value	N	Value	N	Value	N	Value	N	Value	N	Value
2000	4	0.346	0	-	3	0.036	0	-	0	-	0	-	1	0.31	0	-
2001	3	0.16	2	0.021	3	0.16	0	-	0	-	0	-	0	-	2	0.021
2002	13	0.316	1	0.592	9	0.162	1	0.592	1	0.041	0	-	3	0.114	0	-
2003	41	11.09	2	0.033	23	0.545	2	0.033	3	0.013	0	-	15	10.532	0	-
2004	41	1.33	3	0.047	31	0.289	1	0.009	2	0.787	1	0.002	8	0.254	1	0.036
2005	34	0.632	1	0.012	31	0.614	1	0.012	0	-	0	-	3	0.018	0	-
2006	31	4.02	3	1.544	19	1.457	2	1.536	1	2.253	0	-	11	0.31	1	0.008
2007	79	14.659	8	1.076	33	0.531	3	0.764	27	6.897	1	0.061	19	7.231	4	0.25
2008	84	13.636	11	5.054	46	3.146	9	5.013	28	9.055	1	0.034	10	1.435	1	0.006
2009	85	19.068	12	4.75	39	1.572	11	4.716	27	11.234	0	-	19	6.261	1	0.034
Total	415	65.257	43	13.128	237	8.512	30	12.675	89	30.28	3	0.097	89	26.465	10	0.356

Panel B: Time Distribution of Targets by Nation														
Year	AU	CA	CH	FR	HK	ID	JP	MO	NL	SG	TH	TW	US	Total
2001	0	0	0	0	2	0	0	0	0	0	0	0	0	2
2002	0	0	0	0	0	1	0	0	0	0	0	0	0	1
2003	0	0	0	0	2	0	0	0	0	0	0	0	0	2
2004	0	0	0	1	2	0	0	0	0	0	0	0	0	3
2005	0	0	0	0	1	0	0	0	0	0	0	0	0	1
2006	0	0	1	0	1	0	0	0	0	0	0	0	1	3
2007	0	0	0	0	4	0	0	1	1	0	0	0	2	8
2008	2	0	0	0	6	0	0	0	0	1	0	1	1	11
2009	1	1	0	1	4	0	2	0	0	2	1	0	0	12
Total	3	1	1	2	22	1	2	1	1	3	1	1	4	43



Panel C: Time Distribution of Targets by Industry														
Year	CPS	CS	ENERGY	FIN	GOVT	HEALTH	HI-TECH	IND	MAT	ENT	PROP	RETAIL	TELE	Total
Panel C(i): Domestic														
<b>2000</b>	0	2	0	0	0	0	1	0	1	0	0	0	0	<b>4</b>
<b>2001</b>	0	0	0	0	0	0	0	1	1	0	0	0	1	<b>3</b>
<b>2002</b>	0	0	0	1	4	0	1	2	2	0	0	1	2	<b>13</b>
<b>2003</b>	1	3	6	1	0	6	8	3	7	0	3	1	2	<b>41</b>
<b>2004</b>	3	2	6	2	0	9	3	5	4	1	2	1	3	<b>41</b>
<b>2005</b>	1	1	3	1	0	7	3	10	3	1	2	1	1	<b>34</b>
<b>2006</b>	1	2	6	4	0	2	2	2	3	4	5	0	0	<b>31</b>
<b>2007</b>	2	3	10	4	1	8	8	15	10	1	13	3	1	<b>79</b>
<b>2008</b>	4	4	5	3	0	6	17	11	20	3	8	2	1	<b>84</b>
<b>2009</b>	5	3	12	11	0	3	12	14	5	3	14	2	1	<b>85</b>
<b>Total</b>	<b>17</b>	<b>20</b>	<b>48</b>	<b>27</b>	<b>5</b>	<b>41</b>	<b>55</b>	<b>63</b>	<b>56</b>	<b>13</b>	<b>47</b>	<b>11</b>	<b>12</b>	<b>415</b>

Panel C: Time Distribution of Targets by Industry														
Year	CPS	CS	ENERGY	FIN	GOVT	HEALTH	HI-TECH	IND	MAT	ENT	PROP	RETAIL	TELE	Total
Panel C(ii): Foreign														
2001	0	0	0	0	0	0	0	0	0	1	0	0	1	2
2002	0	0	1	0	0	0	0	0	0	0	0	0	0	1
2003	0	0	0	0	0	0	0	0	0	0	0	2	0	2
2004	0	1	0	0	0	0	1	0	1	0	0	0	0	3
2005	0	0	0	0	0	0	1	0	0	0	0	0	0	1
2006	0	0	1	2	0	0	0	0	0	0	0	0	0	3
2007	1	0	0	4	0	0	1	1	1	0	0	0	0	8
2008	1	1	0	2	0	1	0	2	2	1	1	0	0	11
2009	1	0	0	2	0	0	2	3	4	0	0	0	0	12
Total	3	2	2	10	0	1	5	6	8	2	1	2	1	43

**Table 2: Summary Statistics**

This table reports the summary statistics for the full sample. The domestic sample contains those deals where the target was a Chinese firm (Domestic) while the foreign sample relates to those deals where the target was located outside of China (Foreign). The market value (MV) is the market value of the acquirer as measured two months before the announcement of the deal (in billions). The market to book value (MTBV) of the acquirer is measured two months prior to the deal announcement. The variable RUNUP is the stock performance of the acquirer prior to the announcement measured using the CAR [-364, -7]. The acquirer's leverage, measured as the percentage of total debt to total capital, in annual terms, is measured at the year prior to the deal announcement (Leverage). Cash Flows/Total Assets is measured at the year prior to the deal announcement and is calculated as the Funds from Operations divided by the Total Assets of the firm (CF/TA). For additional variables noted in the literature, we consider the cases of acquisitions of publicly listed targets (Public Target); privately held targets (Private Target); Other targets relate to those targets not privately, publicly or state-owned, i.e. subsidiaries and joint-ventures (Other Target); state-owned bidders (SOE Bidder); state-owned targets (SOE Target); deals financed using 100% cash (Cash); 100% stock (Stock); a mixture of cash and stock (Mixed); the number of hostile deals in each sample (Number of Hostile Deals); the number of competed deals in each sample (Number of Competed Deals); the average number of deals conducted by each acquirer (Average Number of Acquirer Deals); the relative transaction value, calculated as the deal value divided by the market value of the bidder as measured two months prior to the deal announcement (Relative Transaction Value), and finally, the bidder's 3-day cumulative announcement abnormal return (CAR (-1,+1)) and 24-month buy-and-hold abnormal return measured from the announcement date (BHAR (0, +24)).

<b>Statistic</b>	<b>Domestic</b>	<b>Foreign</b>
<i>N</i>	415	43
<i>MV</i>	\$1.12 billion	\$22.74 billion
<i>MTBV</i>	6.36	2.83
<i>RUNUP</i>	5.94%	-19.62%
<i>Leverage</i>	29.10%	21.14%
<i>CF/TA</i>	7.60%	17.56%
<i>Public Target</i>	33	12
<i>Private Target</i>	118	14
<i>Other Target</i>	264	17
<i>SOE Bidder</i>	60	7
<i>SOE Target</i>	144	4
<i>Cash</i>	237	30
<i>Stock</i>	89	3
<i>Mixed</i>	89	10
<i>Diversifying Deals</i>	224	25
<i>Number of Hostile Deals</i>	0	0
<i>Number of Competed Deals</i>	0	0
<i>Average Number of Acquirer Deals</i>	1.39	1.30
<i>Relative Transaction Value</i>	48.96%	25.70%
<i>CAR (-1, +1)</i>	2.76%	-0.58%
<i>BHAR (0, +24)</i>	-7.98%	14.20%

**Table 3: Acquirer Short-Term Performance by Size**

This table reports acquirer short-run 3 day cumulative announcement abnormal returns (CARs) for the full sample. We measure the CAR using the formula  $CAR_i = \sum_{t=0}^n AR_i$ . The domestic sample contains those deals where the target was a Chinese firm (Domestic) while the foreign sample relates to those deals where the target was located outside of China (Foreign). Cash deals refer to those deals which were financed 100% using cash (Cash); stock deals refer to those which were financed 100% using equity (Stock); and Mixed deals refer to those deals which were financed using equity and cash (Mixed). Panel A relates to the full sample (Full Sample); Panel B relates to small acquirers as measured as those firms in the lowest one third of bidders once ranked by their market value two months prior to the deal announcement (Small Acquirers); Panel C relates to larger acquirers as measured as those firms in the highest one third of bidders once ranked by their market value two months prior to the deal announcement (Large Acquirers); and Panel D relates to the differential performance between small and large bidders (i.e. Panel B – Panel C). The P-Value is shown in parentheses and is calculated using the t-test for CARs and the Wilcoxon rank-sum test for the difference between the sub-samples. Statistical significance at the 1% level, 5% level and 10% levels is denoted \*\*\*, \*\* and \* respectively.

	Domestic				Foreign				Differential			
	All	Cash	Stock	Mixed	All	Cash	Stock	Mixed	All	Cash	Stock	Mixed
<b>Panel A: Full Sample</b>												
<b>Mean</b>	2.76%***	1.30%***	6.24%***	3.17%***	-0.58%	-0.57%	3.77%	-1.93%	3.34%***	1.86%*	2.47%	5.10%*
<b>P-Value</b>	(0.000)	(0.000)	(0.000)	(0.001)	(0.604)	(0.664)	(0.635)	(0.393)	(0.003)	(0.069)	(0.605)	(0.072)
<b>N</b>	415	237	89	89	43	30	3	10				
<b>Panel B: Small Acquirers</b>												
<b>Mean</b>	3.58%***	1.50%**	8.27%***	3.69%***	-0.36%	-1.66%	6.69%	-1.84%	3.93%**	3.16%	1.57%	5.53%
<b>P-Value</b>	(0.000)	(0.011)	(0.003)	(0.005)	(0.853)	(0.464)	(0.643)	(0.296)	(0.044)	(0.189)	(0.876)	(0.102)
<b>N</b>	139	70	30	39	12	4	2	6				
<b>Panel C: Large Acquirers</b>												
<b>Mean</b>	1.88%***	1.50%***	5.13%***	-0.09%	0.82%	0.57%	-2.07%	8.52%	1.06%	0.93%	7.20%	-8.61%
<b>P-Value</b>	(0.001)	(0.007)	(0.002)	(0.965)	(0.459)	(0.617)	-	-	(0.228)	(0.186)	(0.425)	(0.180)
<b>N</b>	130	86	23	21	21	19	1	1				
<b>Panel D: Differential Performance (Panel B – Panel C)</b>												
<b>Differential</b>	1.69%	0.00%	3.14%	3.78%	-1.18%	-2.23%	8.76%	-10.36%				
<b>P-Value</b>	(0.428)	(0.540)	(0.369)	(0.170)	(0.349)	(0.516)	(1.000)	(0.134)				

**Table 4: Acquirer Short-Term Performance by Industry**

This table reports the short-run acquirer 3 day (-1, +1) cumulative announcement abnormal returns (CARs) stratified by the target industry for the full sample. We measure the CAR using the formula  $CAR_i = \sum_{t=-1}^1 AR_{it}$ . Panel A reports the results for the full sample (Full Sample); Panel B reports the results for acquirers of domestic targets (Domestic); and Panel C reports the results for acquirers of foreign targets (Foreign). The industries are abbreviated as follows: CPS – Consumer Products and Services; STAPLES – Consumer Staples; ENERGY – Energy and Power; FIN = Financials; GOVT – Government and Agencies; HEALTH – Healthcare; HI-TECH – High Technology; IND – Industrials; MAT – Materials; ENT – Media and Entertainment; PROP – Real Estate; RETAIL – Retail; TELE – Telecommunications. The mean CAR is reported with the p-value in parentheses. Significance at the 1% level, 5% level and 10% levels is denoted \*\*\*, \*\* and \* respectively.

	CPS	CS	ENERGY	FIN	GOVT	HEALTH	HI-TECH	IND	MAT	ENT	PROP	RETAIL	TELE
<b>Panel A: Full Sample</b>													
<b>Mean</b>	0.94%	2.53%	3.78%***	2.19%*	4.03%***	2.58%***	0.95%	3.25%***	2.21%***	0.56%	2.46%*	4.42%	3.11%
<b>P-Value</b>	(0.500)	(0.134)	(0.005)	(0.080)	(0.000)	(0.009)	(0.403)	(0.000)	(0.003)	(0.671)	(0.064)	(0.164)	(0.360)
<b>N</b>	20	22	50	37	5	42	60	69	64	15	48	13	13
<b>Panel B: Domestic Deals</b>													
<b>Mean</b>	2.00%	3.17%*	3.74%***	3.39%**	4.03%***	2.66%***	1.35%	3.54%***	1.96%**	0.76%	2.14%	7.83%***	3.64%
<b>P-Value</b>	(0.141)	(0.078)	(0.006)	(0.034)	(0.000)	(0.009)	(0.262)	(0.000)	(0.012)	(0.616)	(0.103)	(0.006)	(0.322)
<b>N</b>	17	20	48	27	5	41	55	63	56	13	47	11	12
<b>Panel C: Foreign Deals</b>													
<b>Mean</b>	-5.05%	-3.95%	4.64%	-1.04%	-	-0.47%	-3.41%	0.23%	3.93%	-0.75%	17.35%	-14.38%	-3.21%
<b>P-Value</b>	(0.389)	(0.445)	(0.681)	(0.520)	-	-	(0.367)	(0.889)	(0.164)	(0.716)	-	-	-
<b>N</b>	3	2	2	10	0	1	5	6	8	2	1	2	1

**Table 5: Acquirer Long-Term Performance by Size**

This table reports the acquirer long-run 24 month Buy-and-Hold Abnormal Returns (BHARs) for the full sample from the announcement date. We measure the buy-and-hold abnormal return using the formula  $BHAR_{it} = \prod_{t=0}^T [1 + R_{it}] - \prod_{t=0}^T [1 + R_{mt}]$ . The domestic sample contains those deals where the target was a Chinese firm (Domestic) while the foreign sample relates to those deals where the target was located outside of China (Foreign). Cash deals refer to those which were financed 100% using cash (Cash); stock deals refer to those which were financed 100% using equity (Stock); and mixed deals refer to those deals with known information confirming that the deal was financed using equity and cash (Mixed). Panel A reports the results for the full sample (Full Sample); Panel B reports the results of small acquirers, measured as the lowest one-third of bidders as ranked by their market value two months prior to the deal announcement (Small Acquirers); Panel C reports the results of large acquirers, measured as the highest one-third of bidders as ranked by their market value two months prior to the deal announcement (Large Acquirers); and Panel D reports the differential performance between small and large bidders (i.e. Panel B – Panel C). The P-Value is shown in parentheses calculated using the bootstrapping method while the Wilcoxon rank-sum test is used for estimating the statistical difference between sub-samples. Significance at the 1% level, 5% level and 10% levels is denoted \*\*\*, \*\* and \* respectively.

	Domestic				Foreign				Differential			
	All	Cash	Stock	Mixed	All	Cash	Stock	Mixed	All	Cash	Stock	Mixed
<b>Panel A: Overall Samples</b>												
<b>Mean</b>	-7.98%**	-10.54%**	9.08%	-18.24%**	14.20%	7.47%	-27.85%	47.00%	-22.18%	-18.01%**	36.93%	-65.24%
<b>P-Value</b>	(0.026)	(0.021)	(0.182)	(0.041)	(0.631)	(0.682)	(0.703)	(0.827)	(0.460)	(0.041)	(0.684)	(0.246)
<b>N</b>	415	237	89	89	43	30	3	10				
<b>Panel B: Small Acquirers</b>												
<b>Mean</b>	-15.57%*	-20.98%*	6.73%	-23.01%	-7.62%	-136.14%	-40.46%	89.02%	-7.95%**	115.16%**	47.19%	-112.02%
<b>P-Value</b>	(0.053)	(0.057)	(0.693)	(0.140)	(0.972)	(0.168)	-	(0.923)	(0.026)	(0.041)	(0.586)	(0.217)
<b>N</b>	139	70	30	39	12	4	2	6				
<b>Panel C: Large Acquirers</b>												
<b>Mean</b>	-7.42%	-8.47%	5.90%	-17.70%*	22.39%***	25.33%***	-2.63%	-8.34%	-29.81%***	-33.80%***	8.53%	-9.37%
<b>P-Value</b>	(0.151)	(0.254)	(0.555)	(0.065)	(0.008)	(0.009)	-	-	(0.005)	(0.001)	(0.514)	(0.813)
<b>N</b>	130	86	23	21	21	19	1	1				
<b>Panel D: Differential Performance (Panel B – Panel C)</b>												
<b>Differential</b>	-8.15%	-12.51%	0.83%	-5.30%	-30.01%***	-161.47%***	-37.84%	97.35%				
<b>P-Value</b>	(0.594)	(0.817)	(0.484)	(0.871)	(0.003)	(0.005)	(1.000)	(0.317)				

**Table 6: Acquirer Long-Term Performance by Industry**

This table reports the acquirer long-run 24-month Buy-and-Hold Abnormal Returns (BHARs) for the full sample from the announcement date stratified by the target industry. We measure the buy-and-hold abnormal return using the formula  $BHAR_{it} = \prod_{t=0}^T [1 + R_{it}] - \prod_{t=0}^T [1 + R_{mt}]$ . Panel A reports the results for the full samples while Panel B refers to acquirers of domestic targets (Domestic Deals) and Panel C to the acquirers of foreign targets outside of China (Foreign). The industries are abbreviated as follows: CPS – Consumer Products and Services; STAPLES – Consumer Staples; ENERGY – Energy and Power; FIN = Financials; GOVT – Government and Agencies; HEALTH – Healthcare; HI-TECH – High Technology; IND – Industrials; MAT – Materials; ENT – Media and Entertainment; PROP – Real Estate; RETAIL – Retail; TELE – Telecommunications. The mean BHAR is reported with the p-value in parentheses. Significance at the 1% level, 5% level and 10% levels is denoted \*\*\*, \*\* and \* respectively.

	CPS	STAPLES	ENERGY	FIN	GOVT	HEALTH	HI-TECH	IND	MAT	ENT	PROP	RETAIL	TELE
<b>Panel A: Overall Sample</b>													
<b>Mean</b>	-21.37%*	-18.70%	1.00%	2.18%	-19.24%***	-4.15%	-8.50%	-15.37%*	-5.15%	24.55%	-1.78%	10.08%	1.86%
<b>P-Value</b>	(0.083)	(0.291)	(0.924)	(0.782)	(0.001)	(0.664)	(0.506)	(0.061)	(0.622)	(0.813)	(0.801)	(0.707)	(0.956)
<b>N</b>	20	22	50	37	5	42	60	69	64	15	48	13	13
<b>Panel B: Domestic Deals</b>													
<b>Mean</b>	-21.10%	-22.19%	3.13%	0.91%	-19.24%***	-4.88%	-8.12%	-15.31%*	-0.81%	-45.06%	-3.21%	24.10%	5.86%
<b>P-Value</b>	(0.110)	(0.223)	(0.741)	(0.932)	(0.001)	(0.618)	(0.517)	(0.064)	(0.939)	(0.122)	(0.652)	(0.415)	(0.872)
<b>N</b>	17	20	48	27	5	41	55	63	56	13	47	11	12
<b>Panel C: Foreign Deals</b>													
<b>Mean</b>	-22.92%	16.21%	-49.92%	5.59%	-	25.92%	-12.67%	-15.94%	-35.48%	477.00%	65.84%	67.07%	-46.15%
<b>P-Value</b>	(0.636)	-	-	(0.602)	-	-	(0.931)	(0.931)	(0.207)	-	-	-	-
<b>N</b>	3	2	2	10	0	1	5	6	8	2	1	2	1

### **Table 7: Short-Run Cross-Sectional Analysis**

This table reports the short-run results for the multivariate analysis of the full sample. In these models we regress acquirer 3 day cumulative announcement abnormal returns (CARs (-1, +1)) against a vector of explanatory variables. These include the following dummy variables which take the value of one - if the target is foreign (Foreign); if the bidder was a state-owned enterprise (SOE Bidder); if the deal was financed using 100% stock (Stock); if the deal was financed using 100% cash (Cash); if the target was publicly listed (Public Target); if the bidder had conducted at least 3 takeovers before the acquisition (Experienced Bidder); if the deal was conducted after RMB exchange rate reform from 21st July, 2005 (Currency Appreciation); if the bidder was in a high-valuation market (High-Valuation Market) or in a low-valuation market (Low-Valuation Market); and finally, if the target was in a different industry to the bidder as measured using the first two digits of the four digit Primary SIC code of the two firms (Diversifying). We also include the following continuous variables: the acquirer's market-to-book value (MTBV); the acquirer size (LN(MV)) measured two months prior to the announcement of the deal; the acquirer pre-announcement stock performance as measured using the CAR over the window [-364, -7] (RUNUP); the acquirer's leverage (Leverage), measured one year pre-announcement as the percentage of annual total debt to annual total capital; the acquirer's Cash Flows/Total Assets (CF/TA) measured one year pre-announcement as the funds from operations divided by the total assets of the firm; the moving average MA(4) of the number of M&As announced in each quarter divided by the historic average of the M&As announced in all previous quarters spanning back until 1995 (Market Heat); finally, we include the relative size of the deal (Relative Size) measured two-months pre-announcement as the deal value divided by the acquirer's market value. All continuous variables are winsorized at the 1% and 99% levels. Bidder and target industry dummies and fixed-year effects are also controlled for but for brevity, they are not reported in the table. The P-Value shown in parentheses is adjusted for heteroskedasticity and bidder clustering. Significance at the 1% level, 5% level and 10% is denoted \*\*\*, \*\* and \* respectively.



	(1)	(2)	(3)
<b>Foreign</b>	-0.0273*	-0.0271*	-0.0286**
	(0.051)	(0.053)	(0.047)
<b>SOE Bidder</b>	0.0153	0.0150	0.0151
	(0.121)	(0.128)	(0.127)
<b>Stock</b>	0.0099	0.0179	
	(0.489)	(0.148)	
<b>Cash</b>	-0.0129		-0.0169**
	(0.143)		(0.027)
<b>Public Target</b>	0.0166	0.0156	0.0175
	(0.164)	(0.185)	(0.133)
<b>Experienced Bidder</b>	0.0006	0.0004	0.0007
	(0.935)	(0.959)	(0.925)
<b>Currency Appreciation</b>	0.0201	0.0158	0.0209
	(0.556)	(0.639)	(0.543)
<b>High Valuation Markets</b>	0.0018	0.0006	0.0017
	(0.880)	(0.961)	(0.886)
<b>Low Valuation Markets</b>	-0.0028	-0.0019	-0.0035
	(0.786)	(0.854)	(0.739)
<b>Market Heat</b>	0.0287	0.0249	0.0296
	(0.420)	(0.482)	(0.408)
<b>Diversifying</b>	0.0018	0.0012	0.0024
	(0.813)	(0.875)	(0.747)
<b>MTBV</b>	-0.0010	-0.0008	-0.0010
	(0.249)	(0.326)	(0.247)
<b>LN(MV)</b>	-0.0026	-0.0032	-0.0026
	(0.382)	(0.280)	(0.388)
<b>RUNUP</b>	0.0099	0.0104	0.0100
	(0.218)	(0.198)	(0.218)
<b>Leverage</b>	-0.0429**	-0.0431**	-0.0429**
	(0.014)	(0.014)	(0.015)
<b>CF/TA</b>	-0.0874	-0.0864	-0.0876
	(0.143)	(0.151)	(0.139)
<b>Relative Size</b>	0.0100**	0.0106**	0.0105**
	(0.023)	(0.018)	(0.014)
<b>Constant</b>	0.0920	0.1000	0.0893
	(0.188)	(0.147)	(0.204)
<i>N</i>	458	458	458
<i>R</i> <sup>2</sup>	0.236	0.232	0.234

**Table 8: Long-Run Cross-Sectional Analysis**

This table reports the long-run results for the multivariate analysis of the full sample. In these models we regress acquirer 24 month post-announcement buy-and-hold abnormal returns (BHARs (0, +24)) against a vector of explanatory variables. These include the following dummy variables which take the value of one - if the target is foreign (Foreign); if the bidder was a state-owned enterprise (SOE Bidder); if the deal was financed using 100% stock (Stock); if the deal was financed using 100% cash (Cash); if the target was publicly listed (Public Target); if the bidder had conducted at least 3 takeovers before the acquisition (Experienced Bidder); if the deal was conducted after RMB exchange rate reform from 21st July, 2005 (Currency Appreciation); if the bidder was in a high-valuation market (High-Valuation Market) or in a low-valuation market (Low-Valuation Market); and finally, if the target was in a different industry to the bidder as measured using the first two digits of the four digit Primary SIC code of the two firms (Diversifying). We also include the following continuous variables: the acquirer's market-to-book value (MTBV); the acquirer size (LN(MV)) measured two months prior to the announcement of the deal; the acquirer pre-announcement stock performance as measured using the CAR over the window [-364, -7] (RUNUP); the acquirer's leverage (Leverage), measured one year pre-announcement as the percentage of annual total debt to annual total capital; the acquirer's Cash Flows/Total Assets (CF/TA) measured one year pre-announcement as the funds from operations divided by the total assets of the firm; the moving average MA(4) of the number of M&As announced in each quarter divided by the historic average of the M&As announced in all previous quarters spanning back until 1995 (Market Heat); finally, we include the relative size of the deal (Relative Size) measured two-months pre-announcement as the deal value divided by the acquirer's market value. All continuous variables are winsorized at the 1% and 99% levels. Bidder and target industry dummies and fixed-year effects are also controlled for but for brevity, they are not reported in the table. The P-Value shown in parentheses is adjusted for heteroskedasticity and bidder clustering. Significance at the 1% level, 5% level and 10% is denoted \*\*\*, \*\* and \* respectively.

	(1)	(2)	(3)
<b>Foreign</b>	0.0637 (0.686)	0.0605 (0.703)	0.0289 (0.855)
<b>SOE Bidder</b>	0.2240** (0.039)	0.2280** (0.034)	0.2170** (0.045)
<b>Stock</b>	0.2650*** (0.009)	0.1640* (0.075)	
<b>Cash</b>	0.1610* (0.081)		0.0521 (0.529)
<b>Public Target</b>	0.2590* (0.059)	0.2710* (0.053)	0.2840** (0.035)
<b>Experienced Bidder</b>	-0.1510* (0.081)	-0.1480* (0.088)	-0.1490* (0.088)
<b>Currency Appreciation</b>	-0.0760 (0.877)	-0.0215 (0.965)	-0.0560 (0.909)
<b>High Valuation Markets</b>	-0.1270 (0.196)	-0.1120 (0.249)	-0.1290 (0.192)
<b>Low Valuation Markets</b>	-0.1590 (0.255)	-0.1710 (0.228)	-0.1770 (0.209)
<b>Market Heat</b>	0.0157 (0.957)	0.0642 (0.831)	0.0382 (0.897)
<b>Diversifying</b>	-0.0965 (0.235)	-0.0891 (0.266)	-0.0787 (0.330)
<b>MTBV</b>	0.0025 (0.719)	0.0009 (0.901)	0.0026 (0.712)
<b>LN(MV)</b>	0.0924** (0.018)	0.0996** (0.011)	0.0928** (0.022)
<b>RUNUP</b>	0.0778 (0.242)	0.0712 (0.282)	0.0808 (0.226)
<b>Leverage</b>	0.1650 (0.383)	0.1670 (0.376)	0.1660 (0.388)
<b>CF/TA</b>	-0.7990 (0.265)	-0.8110 (0.263)	-0.8050 (0.267)
<b>Relative Size</b>	0.0759* (0.058)	0.0683* (0.088)	0.0884** (0.032)
<b>Constant</b>	-1.3430** (0.020)	-1.4440 (0.015)	-1.4150** (0.016)
<i>N</i>	458	458	458
<i>R</i> <sup>2</sup>	0.202	0.196	0.191